

## CREDIT OPINION

21 January 2022



### Contacts

Nicholas Lehman +1.617.535.7694  
 VP-Senior Analyst  
 nicholas.lehman@moody's.com

Lauren Von Bargaen +1.212.553.4491  
 AVP-Analyst  
 lauren.vonbargaen@moody's.com

### CLIENT SERVICES

Americas 1-212-553-1653  
 Asia Pacific 852-3551-3077  
 Japan 81-3-5408-4100  
 EMEA 44-20-7772-5454

# Newton (City of) MA

## Update to credit analysis

### Summary

[Newton](#) (Aaa stable) benefits from a large and wealthy tax base that favorably borders the City of Boston (Aaa stable) to the west. Though primarily residential in nature, the economy is diverse with a large amount of commercial as well as an institutional presence. The city's financial position is stable and benefits from strong fiscal management although reserves will remain below national and regional peers for the highest rating category. The debt burden is average and the city maintains an aggressive funding schedule toward unfunded pension and OPEB liabilities.

### Credit strengths

- » Large, wealthy and diverse tax base with favorable location and institutional presence
- » Strong fiscal management including five-year forecasting and capital planning with formal policies
- » History of taxpayer support for debt exclusions and general overrides to the tax levy limit

### Credit challenges

- » Below-average reserves and liquidity as a percent of revenue
- » Limited ability to raise property tax levy limit under Proposition 2 ½
- » Large long-term liabilities for pension and OPEB

### Rating outlook

The stable outlook reflects Moody's expectation of continued financial stability due to conservative five-year budget forecast and capital improvement plan as well as adherence to comprehensive fiscal policies. The outlook also incorporates the ongoing strength in the city's tax base and economy.

### Factors that could lead to an upgrade

- » Not applicable

### Factors that could lead to a downgrade

- » Decline in available general fund reserves
- » Increase in use of reserves to balance the operating budget

- » Material increase in the debt burden
- » Material increase in the unfunded pension and OPEB liabilities

## Key indicators

Exhibit 1

### Newton (City of) MA

	2016	2017	2018	2019	2020
<b>Economy/Tax Base</b>					
Total Full Value (\$000)	\$22,305,254	\$26,223,774	\$26,223,774	\$30,006,442	\$30,006,442
Population	88,317	88,479	88,660	88,593	88,593
Full Value Per Capita	\$252,559	\$296,384	\$295,779	\$338,700	\$338,700
Median Family Income (% of US Median)	251.4%	250.4%	246.2%	244.8%	244.8%
<b>Finances</b>					
Operating Revenue (\$000)	\$373,457	\$426,285	\$442,866	\$461,493	\$484,643
Fund Balance (\$000)	\$54,644	\$63,493	\$64,087	\$68,590	\$70,595
Cash Balance (\$000)	\$81,212	\$88,975	\$89,558	\$93,947	\$103,046
Fund Balance as a % of Revenues	14.6%	14.9%	14.5%	14.9%	14.6%
Cash Balance as a % of Revenues	21.7%	20.9%	20.2%	20.4%	21.3%
<b>Debt/Pensions</b>					
Net Direct Debt (\$000)	\$260,150	\$284,825	\$297,287	\$290,505	\$308,486
3-Year Average of Moody's ANPL (\$000)	\$527,267	\$557,706	\$568,201	\$575,063	\$597,734
Net Direct Debt / Full Value (%)	1.2%	1.1%	1.1%	1.0%	1.0%
Net Direct Debt / Operating Revenues (x)	0.7x	0.7x	0.7x	0.6x	0.6x
Moody's - ANPL (3-yr average) to Full Value (%)	2.4%	2.1%	2.2%	1.9%	2.0%
Moody's - ANPL (3-yr average) to Revenues (x)	1.4x	1.3x	1.3x	1.2x	1.2x

As of June 30 fiscal year-end

Sources: US Census Bureau, Newton (City of) MA's financial statements and Moody's Investors Service

## Profile

Newton is located seven miles west and borders the City of Boston (Aaa stable). The city has a population of 88,593 (2019 American Community Survey) and a tax base that is primarily residential but benefits from a diverse commercial presence.

## Detailed credit considerations

### Economy and tax base: healthy valuation growth, diverse economy and strong wealth continue to support highest rating category

Newton's economy and tax base will likely remain stable over the next few years given continued valuation growth driven by a strong residential housing market, new development and a diverse commercial sector. The \$33.7 billion tax base (2021-22 equalized value) increased by 12.4% from the 2019 two-year certification. Additionally, the 2022 assessed value increased by 6.7% bringing the five year annual growth rate to 5.9%. Two of the city's larger development projects continue to move forward. The Northland mixed used project passed a referendum in March 2020 and includes 800 residential units, 180,000 square feet of office space and 115,000 square feet of retail space with construction anticipated to begin in the next year. While the Riverside mixed use project at the location of the commuter rail station is beginning construction this year. The transit-oriented project includes over 1 million square feet of office, retail, housing. The project also includes two new life science buildings, and a parking garage.

The local economy is bolstered by institutional presence including [Boston College](#) (Aa3 stable) and a large healthcare presence with Newton-Wellesley Hospital, a member of the [Mass General Brigham Incorporated, MA](#) (Aa3 stable). The city benefits from favorable access to three MBTA stations, all of which are undergoing repairs and renovations by the commonwealth.

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Resident income and wealth is very strong with a median family income equal to 245% of the US median and \$380,779 2022 equalized value per capita. The city's unemployment rate of 3.4% (November 2021) is healthy and continues to trend below the commonwealth's 4.8% and the US's 3.9%.

#### **Financial operations and reserves: stability and strong fiscal management help mitigate below-average reserves**

The city's financial position will remain stable over the next few years because of strong fiscal management that includes proactive conservative budgeting. Historically, the city has also benefited from added revenue flexibility provided by taxpayers support of general overrides and debt exclusions to the tax levy limit. The city's general fund reserves will also remain stable and have gradually increased over the last five years. Although, the reserves as a percent of revenue are notably smaller than those of other Aaa rated cities in Massachusetts and nationally.

The city's draft audited financial statements for fiscal 2021 reflect an \$11.1 million surplus in the general fund due to conservative budgeting. The conservative budgeting led to reduction in all local revenue including meals and room taxes, building permits and other economically sensitive revenue. The year ended with positive variance to budget in revenue from strong property tax collections, license and permits, motor vehicle excise and intergovernmental. The city also experienced positive variance in expenses from all major departments. The surplus increased the available general fund balance to \$81.99 million representing 16.2% of general fund revenue. The primary revenue source is property taxes representing 75% of fiscal 2021 general fund revenue.

The fiscal 2022 budget increased by 5.2% driven by education, pension and OPEB contributions, salaries and benefits. The budget is balanced with a 4.1% increase in the tax levy and \$4.6 million in ARPA funding as a revenue loss supplement. Year-to-date operations are on budget. The city is managing ongoing challenges from supply chain delays and labor shortages that are around 7% to 8% vacancy rate, which is double the historical level. To date, the city has also committed \$18 million of a total \$63 million in ARPA funding. The commitments so far including funding for school operations and capital needs, city infrastructure projects, public safety, children's library and senior community center.

Newton's financial forecast for fiscal years 2023-27 projects a 3.6% average annual increase in operating revenue and use of \$1.5 million annually from free cash. The forecast reflects budgeted deficits of less than half a percent of revenue in fiscal 2023 that grow to 2.7% of revenue in fiscal 2027. We expect the city to manage the forecast deficits as the budget year approaches based on historical results.

#### **Liquidity**

Cash and equivalents based on draft audited fiscal 2021 results were \$106.1 million representing 21% of general fund revenue.

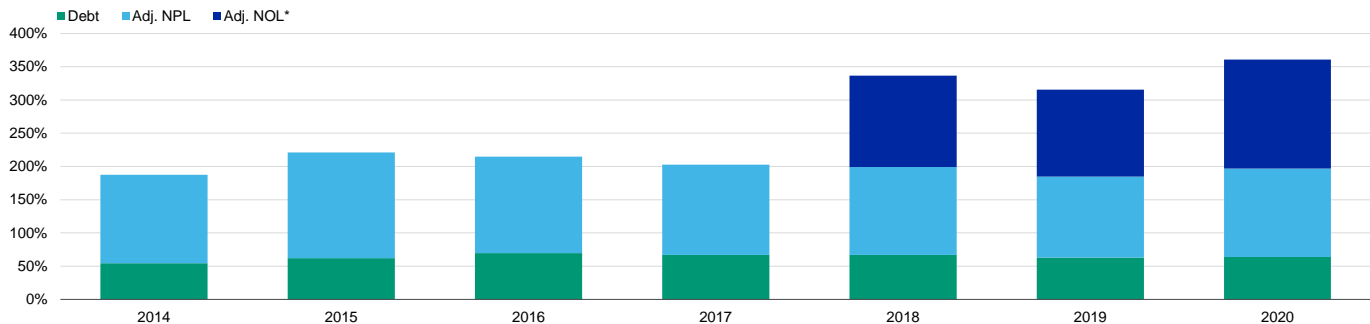
#### **Debt and long-term liabilities: leverage is average for the rating category and well managed**

The city's debt burden and unfunded pension and OPEB liabilities are average for the rating category (see exhibit) and expected to remain manageable given conservative planning and commitment to funding pension and OPEB funding levels. The direct debt burden of \$303 million including the 2022 issuance and excluding self-supporting enterprise debt represents 0.9% of equalized value and 0.6 times general fund revenue. The fiscal 2023-27 capital improvement plan totals \$378.8 million with the potential for \$106.5 million to be funded or partially funded with bonds.

Exhibit 2

**Newton's leverage driven by large but manageable unfunded pension and OPEB liabilities**

Leverage as a % of revenue



Adj. NOL not available pre-GASB 75

Source: Moody's Investors Service and Newton's audited financial statements

**Legal security**

Bonds are backed by the city's full faith and credit, general obligation unlimited tax or limited tax pledge depending on if all of the debt service has been voted by the city to be excluded from the tax levy limit or not.

**Debt structure**

The entire debt portfolio is fixed rate with 52% of principal retired in 10 years. Fiscal 2021 debt service was \$25.1 million representing 5.1% of general fund expenditures.

**Debt-related derivatives**

Newton has no debt-related derivatives.

**Pensions and OPEB**

Newton's pension and OPEB liabilities are larger than the debt burden and, though manageable at this time, represent a potential future credit challenge. The city participates in the Newton Contributory Retirement System, a multi-employer defined benefit plan and makes annual required contributions based on at least its proportional share. The retirement plan expects to be fully funded by 2031 and currently uses a 7.25% discount rate. The city's teachers participate in the Massachusetts Teachers Retirement System in which the city receives on-behalf payments toward the liability that is covered by the Commonwealth. The city also funds its OPEB liability on a pay-go basis plus annual budgeted deposits into an OPEB trust. The OPEB plan fiduciary net position is 2.5% of the total OPEB liability as of the end of fiscal 2021. The table below summarizes the city's 2020 debt, pension and OPEB unfunded liabilities and contributions.

Exhibit 3

**Newton's fiscal 2020 debt, pension and OPEB unfunded liabilities and contributions**

2020	\$\$\$ (000)	% of Operating Revenues	Discount Rate
Operating Revenue	484,643	n/a	n/a
Reported Unfunded Pension Liability	296,245	61%	7.25%
Moody's Adjusted Net Pension Liability	646,405	133%	3.22%
Reported Net OPEB Liability	869,618	179%	2.21%
Moody's Adjusted Net OPEB Liability	793,553	164%	2.70%
Net Direct Debt	308,486	64%	n/a
Debt & unfunded retirement benefits (Moody's adjusted)	1,748,445	360.77%	
Pension Contribution	30,493	6.29%	n/a
OPEB Contribution	26,980	5.57%	n/a
Debt Service	24,459	5.05%	n/a
Total Fixed Costs	81,932	16.91%	n/a
Tread Water Gap	(2,904)	-0.60%	n/a
Moody's Adjusted Fixed Costs	79,029	16.31%	n/a

Source: Moody's Investors Service and Newton's audited financial statements

The city's annual pension contributions over the last five fiscal years 2017-20 have averaged 104% of the tread water indicator, which is the amount required to keep the unfunded liability from increasing if all actuarial assumptions are realized. Failure to realize the assumed return on pension assets could result in larger required increases to meet the funding schedule. Annual pension contributions are scheduled to increase by 9.6% annually. In fiscal 2021 the city adjusted the pension contribution by increasing it by just 4.8% from 2020 to provide some budget flexibility to mitigate coronavirus pandemic impacts. However, the fiscal 2022 pension contribution increased by the scheduled 9.6% plus another 4.8% to bring the funding plan back on schedule from 2021. Newton's fixed costs are also manageable representing less than 17% of revenue.

**ESG considerations****Environmental**

Environmental risk is not material to the city at this time. Moody's ESG Solutions assesses the city's environmental risks based on county level data as having a high risk for hurricanes, medium risk for water stress, extreme rainfall and sea level rise and low risk for heat stress. In response to climate change, city management has developed a comprehensive climate action plan that puts the city on a path to being carbon neutral by 2050. Actions to reduce the city's greenhouse gas emissions include promoting clean, renewable electricity production and consumption, advancing green building construction, and rehabilitating existing buildings.

**Social**

Social considerations are incorporated into the city's economy and tax base discussion above. In addition, the city is focused on improving affordable housing opportunities in the city and this challenge is incorporated into economic development efforts on an ongoing basis.

**Governance**

The city's fiscal management is very strong. The city maintains a five-year financial forecast and capital improvement plan and adheres to formal fiscal policies.

Massachusetts cities have an institutional framework score <sup>1</sup> of "Aa", which is strong. The sector's major revenue source of property taxes, are subject to the Proposition 2 1/2 tax levy cap which can be overridden with voter approval only. However, the cap of 2.5%

still allows for moderate revenue-raising ability. Expenditures primarily consist of personnel costs, as well as education costs for cities that manage school operations, and are highly predictable given state-mandated school spending guidelines and employee contracts. Unpredictable revenue fluctuations tend to be minor, or under 5% annually. Across the sector, fixed costs are generally less than 25% of expenditures. Fixed costs are driven mainly by debt service and pension costs. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

## Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 4

### Newton (City of) MA

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Scorecard Factors and Subfactors	Measure	Score
Economy/Tax Base (30%) <sup>[1]</sup>		
Tax Base Size: Full Value (in 000s)	\$33,734,313	Aaa
Full Value Per Capita	\$380,779	Aaa
Median Family Income (% of US Median)	244.8%	Aaa
Notching Adjustments: <sup>[2]</sup>		
Other Scorecard Adjustment Related to Economy/Tax Base: taxpayer support for debt exclusions and overrides to tax levy limit		Up
Finances (30%)		
Fund Balance as a % of Revenues	16.2%	Aa
5-Year Dollar Change in Fund Balance as % of Revenues	5.4%	A
Cash Balance as a % of Revenues	21.0%	Aa
5-Year Dollar Change in Cash Balance as % of Revenues	4.9%	A
Management (20%)		
Institutional Framework	Aa	Aa
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures (x)	1.0x	A
Notching Adjustments: <sup>[2]</sup>		
Unusually Strong or Weak Budgetary Management and Planning: strong budgetary management		Up
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	0.9%	Aa
Net Direct Debt / Operating Revenues (x)	0.6x	Aa
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	1.9%	Aa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.3x	A
Scorecard-Indicated Outcome		Aa1
Assigned Rating		Aaa

[1] Economy measures are based on data from the most recent year available.

[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.

[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.

Sources: US Census Bureau, Newton's financial statements and Moody's Investors Service

## Endnotes

- 1 The institutional framework score assesses a municipality's legal ability to match revenue with expenditures based on its constitutionally and legislatively conferred powers and responsibilities. See [US Local Government General Obligation Debt \(July 2020\)](#) methodology report for more details.

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